VZCZCXRO4048
PP RUEHCHI RUEHDT RUEHFK RUEHHM RUEHKSO RUEHNAG RUEHNH RUEHPB
DE RUEHHI #0738/01 1721019
ZNR UUUUU ZZH
P 201019Z JUN 08
FM AMEMBASSY HANOI
TO RUEHC/SECSTATE WASHDC PRIORITY 8055
INFO RUEHHM/AMCONSUL HO CHI MINH 4880
RUEHGP/AMEMBASSY SINGAPORE 2620
RUCNASE/ASEAN MEMBER COLLECTIVE
RUEHZU/ASIAN PACIFIC ECONOMIC COOPERATION
RUEATRS/DEPT OF TREASURY WASHINGTON DC
RUCPDOC/DEPT OF COMMERCE WASHINGTON DC

UNCLAS SECTION 01 OF 02 HANOI 000738

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E.O. 12958: N/A
TAGS: ETRD ECON EIND EINV VM
SUBJECT: FOCUS ON U.S. BUSINESS IN VIETNAM: DISTRIBUTION RIGHTS;
LUXURY TAXES ON AUTOMOBILES

REF: A) Hanoi 358
B) Hanoi 451
C) AmCham Vietnam June 19 Letter to Secretary Gutierrez
D) Hanoi 475
E) Hanoi 297

HANOI 00000738 001.2 OF 002

¶1. (U) This cable is sensitive but unclassified. For official use only, not for dissemination outside USG channels or posting on the internet.

¶2. (U) This cable is the first in a series focusing on issues on the U.S. private sector and business agenda in Vietnam.

¶3. (SBU) Summary: The issue of distribution rights has been one of the most contested areas between the Government of Vietnam (GVN) and the private sector here. After the GVN addressed this issue earlier this year, the American Chamber of Commerce (AmCham) in Vietnam has now zeroed in on a subjective "economic needs test" ("ENT") that weighs over prospective retailers. Despite the potentially broad scope of this test, the GVN has applied it narrowly thus far. Another issue is taxes on automobiles. Ford and GM have criticized the GVN for the instability caused by flip-flops on tariffs and proposed hikes in luxury taxes. Embassy Hanoi is working with the private sector and the GVN to promoted transparency. End summary.

DISTRIBUTION: PREMATURE FEARS OF BEING PUT TO THE "TEST"
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¶4. (U) The issue of distribution rights has dominated the U.S. business agenda for most of the last year (Ref A). After MOIT lifted the restriction on the choice of distributors in April 2008 (Ref B), some in the business community have turned their sights on a distribution sector clause commonly known as the "economic needs test" ("ENT"). AmCham is concerned that the GVN could misuse ENT to restrict market access. Thus, ENT concerns were at the top of AmCham's agenda at the May Vietnam Business Forum and featured in a June 19 letter to the Secretary of Commerce (Ref C).

WHO IS COVERED BY THE ECONOMIC NEEDS TEST?

¶5. (SBU) According to existing Vietnamese regulations, prospective foreign businesses must get specific approval based on the size, location and "impact" (or need) of second and subsequent "retail outlets." ENT does not apply to a first establishment. Ambiguities in the law as to what this test on impact or needs entails and who it applies to are at the center of U.S. business concerns. AmCham

has asked the GVN to narrow the scope of ENT by excluding industrial sales and other instances that could be considered retail (Ref C). The GVN, so far, appears currently to be applying an even narrower interpretation of the ENT. The Ministry of Industry and Trade (MOIT), which drew up the regulations, has told post (most recently on June 10) that the ENT only applies to shopping malls and large retail stores (like supermarkets and department stores).

WHAT THE TEST ENTAILS

¶6. (SBU) The issue of what ENT entails poses another problem. The MOIT has told post and USTR that it approaches ENT from a zoning point of view, to deal with such issues as requirements for sufficient parking space, bathroom facilities and the like. TMOIT showed us a second store application from Malaysian retailer Parkson, however, which required it to show the "social and economic impact" that its new outlet would have. Existing regulations also state that applications will be considered on a "case by case basis" and require applicants to demonstrate how the second outlet fits in with a region's "master plan," even though there are provinces and cities that do not have one. The country representative from an American investment consultant brushed aside fears from this subjective test. "Investment applications have the same requirement, and it's never been a problem," he told us. "Sure, it's subjective and sometimes provincial authorities don't understand it, but in the end they always do the right thing and issue the permit."

¶7. (U) Post is working with AmCham on how best to address its members' concerns, and has raised them numerous times with the GVN. For example, at the December 2007 TIFA, Econoff and USTR counterparts urged the GVN to switch to a zone-based system and discard the ENT. We continue to press this point or to at least get

the GVN to commit to the narrowest application of the test.

NO NEW REGULATORY SCHEME

¶8. (U) Another question posed by U.S. businesses interested in entering the distribution sector is what type of regulatory scheme does the GVN intend to introduce in 2009, when the sector opens up for fully foreign-owned businesses. (Vietnam opened the sector to majority foreign businesses-owned joint ventures in January 2008). The answer is none. MOIT's Office of Planning and Investment, which prepares enacting regulations, told us that the regulatory scheme in place sufficed for the time being and that they did not envision new regulations to open up the market in 2009.

THE AUTO INDUSTRY SEEKS REGULATORY STABILITY

¶9. (U) In August 2007, the GVN lowered tariffs on auto imports twice in the space of three months, bringing them down from 80 to 60 percent (Refs D and E). Subsequently, car imports shot up by 70 percent from October 2007 to March 2008. Foreign automakers in Vietnam started importing completely-built units (CBUs) to cash in on the rush and make up for lost price competitiveness on their locally-made models. Then, in March 2008, the GVN did an about face, and brought tariffs up again to 70 percent and then to 83 percent in April.

¶10. (SBU) Moreover, in May 2008 the GVN announced that it would also hike up luxury taxes on locally-made cars and on parts which the foreign automakers import to assemble cars here. Taxes on popular models, like General Motors' Captiva and Ford's Everest (both SUVs), would double to 60 percent. The GVN plans to introduce legislation to raise luxury taxes (known in Vietnam as the Special Consumption Tax) in the next legislative session in October 2008.

¶11. (SBU) The general managers of GM and Ford, both based in Hanoi, told post that they support Vietnam's Auto Manufacturer's Association stance against changes in the luxury tax regime, but that what is most important to them is to have stability in tariff

and tax policy. Ford and GM are concerned that the see-saws on tariffs and taxes are hindering their ability to adopt and follow a mid-term business plan in Vietnam. They say that their businesses could digest the proposed luxury tax regime, as long as the GVN holds firm to its promise to introduce them in 2010.

¶12. (U) In addition to liaising with GM and Ford, post has been in close contact with the Ministry of Finance, which is drafting the luxury tax legislation, and other relevant ministries on this issue. For example, when earlier in May 2008 the automakers became concerned that the GVN would introduce luxury taxes in the June legislative session, the Ministry of Finance told the Ambassador that the plan would not be rushed. The U.S. automakers are also engaged with the GVN and are optimistic that their concerns will eventually be factored in into whatever scheme the GVN eventually decides to enact.

¶13. (SBU) Comment: Vague regulations have not helped the understanding of distribution rights in Vietnam (Refs A and B). The ENT is an issue that, at least in practice, so far appears to weigh exclusively over department stores and supermarkets, which are dominated by non-American investors. The Europeans do have department stores and supermarkets, including multiple outlets -- but our EU colleagues tell us that they have not faced problems with ENT and that it is not at the top of their agenda. While concerned about tariff and tax instability, the auto industry remains optimistic. Car sales remain strong, rising 106 percent in May from the same period in 2007. In the meantime, we will continue to press the GVN on regulatory stability and transparency and encourage it to abandon the economic needs test. End Comment.

MICHALAK